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Best's Company Report for  
WESTCHESTER SURPLUS LINES INSURANCE COMPANY

Group Affiliation: ACE INA Group

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## BEST'S RATING

Based on our opinion of the company's Financial Strength and relationship with an affiliated reinsurer, which reinsures virtually all of the company's business, the company is assigned the Best's Rating of its affiliated reinsurer, Westchester Fire Insurance Company, which is A (Excellent). The company is assigned the Financial Size Category of Class X, which is the Financial Size Category of its affiliated reinsurer.

## RATING RATIONALE

The following text is derived from the report of ACE Westchester Specialty Group.

**Rating Rationale:** This rating applies to ACE Westchester Specialty Group led by Westchester Fire Insurance Company, along with reinsured members, Westchester Surplus Lines Insurance Company, a non-admitted carrier and Industrial Underwriters Insurance Company. The rating reflects the group's solid capitalization, favorable operating results, strong management and excellent broker relations. The rating outlook is stable.

The strengths are derived from management's successful operating strategies and the group's strategic role, along with the ACE American Pool, as the U.S. arm of Bermuda-based ACE Limited, a leading worldwide insurer. ACE Limited's significant financial resources and name recognition have enhanced the group's business opportunities as strategic initiatives put into place to grow and rebalance the group's book of business have resulted in significantly increased income over the past three years. Also, the group's capitalization is enhanced by the additional financial flexibility and access to capital through ACE Limited, which maintains consolidated GAAP equity of approximately \$8.8 billion. Furthermore, the group's capital is provided additional protection through an adverse development cover with National Indemnity Company, a subsidiary of Berkshire Hathaway, Inc. (NICO) on pre-1997 Westchester business.

Prospectively, management strategies include consistent focus on underwriting profits through careful risk selection and pricing, the use of reinsurance to manage net retained exposures to individual losses and loss accumulations as well as ongoing attention to cost control. Operationally, the ACE Westchester group benefits from cross-selling opportunities as a member of the ACE Limited group. ACE Limited is a leading provider of professional liability, excess liability, property and specialty coverages to Fortune 500 and multinational corporate clients. The group's superior management team provides experience, a disciplined underwriting approach and strong claims management capabilities.

These strengths are partially offset by ongoing competitive market conditions. A.M. Best believes that the group continues to be well positioned to benefit from the opportunities presented with changing market conditions and expects continued favorable operating results.

Best's Rating: A r

Outlook: Stable

## FIVE YEAR RATING HISTORY

<u>Date</u>	<u>Best's Rating</u>
06/17/04	A r
06/10/03	A r
03/14/02	A r
01/16/01	A r
08/18/99	A r

## KEY FINANCIAL INDICATORS

<u>Period Ending</u>	<u>Statutory Data (\$000)</u>		<u>Pretax Operating Income</u>
	<u>Direct</u>	<u>Net</u>	
	<u>Premiums Written</u>	<u>Premiums Written</u>	
2000	65,844	6,861	-4,529
2001	178,597	15,073	9,445
2002	504,395	47,171	18,180
2003	530,247	31,280	20,103
2004	644,560	45,784	17,186
03/2004	126,666	9,335	4,493
03/2005	164,463	10,864	5,752

<u>Period Ending</u>	<u>Statutory Data (\$000)</u>		<u>Policy- holders' Surplus</u>
	<u>Net</u>	<u>Total</u>	
	<u>Income</u>	<u>Admitted Assets</u>	
2000	-3,076	79,066	24,617
2001	7,085	141,197	30,798
2002	10,822	201,819	65,283
2003	12,586	288,224	67,847
2004	12,038	367,023	65,420
03/2004	3,693	313,805	74,177
03/2005	3,733	380,146	68,926

<u>Period Ending</u>	<u>Profitability</u>			<u>Leverage</u>		<u>Liquidity</u>		
	<u>Comb.</u>	<u>Inv.</u>	<u>Pretax</u>	<u>NA Inv</u>	<u>NPW</u>	<u>Net</u>	<u>Overall</u>	<u>Oper.</u>
	<u>Ratio</u>	<u>Yield</u>	<u>ROR</u>	<u>Lev</u>	<u>to PHS</u>	<u>Lev</u>	<u>Liq</u>	<u>Cash- flow (%)</u>
2000	310.9	6.9	-99.9	3.4	0.3	2.4	148.4	-32.5
2001	9.2	5.4	109.8	1.7	0.5	4.0	129.9	238.4
2002	50.2	4.2	52.2	0.0	0.7	2.8	150.5	140.8
2003	82.3	3.4	53.3	...	0.5	3.6	136.9	139.6
2004	67.7	4.2	44.3	0.1	0.7	5.0	131.8	200.9
5-Yr Avg	70.6	4.5	48.8	...	...	...	...	...
03/2004	69.3	XX	49.7	XX	0.4	3.5	136.5	999.9
03/2005	73.7	XX	51.7	XX	0.7	4.9	132.0	100.7

(\*) Data reflected within all tables of this report has been compiled from the company-filed statutory statement. Within several financial tables of this report, this company is compared against the Professional Surplus Lines Writers.

## BUSINESS REVIEW

The following text is derived from the report of ACE Westchester Specialty Group.

Since being acquired by Bermuda-based ACE Limited, ACE Westchester is part of one of the largest global insurance organizations in the world and ranks among the twenty largest commercial lines insurance organizations in the U.S. ACE Westchester specializes in the wholesale distribution of excess and surplus lines property, inland marine, casualty and professional

lines products and also provides coverage for agriculture business and specialty programs.

Current operations managed by ACE Westchester are organized into two business units offering highly specialized products and services: ACE Westchester Specialty Division and ACE Programs Division. The ACE Westchester Specialty Division focuses on wholesale distribution of excess, surplus and specialty property, inland marine, casualty and professional lines products. In addition, the ACE Programs Division provides insurance coverage to commercial, specialty homeowners and agriculture markets.

**Direct Premium Writings By Product Lines:** Direct Premiums written at the last year end totaled (\$000) \$ 644,560, and were distributed as follows: Allied Lines, \$ 134,986; Fire, \$ 125,118; Oth Liab Occur, \$ 157,073; Oth Liab Cl-Made, \$ 36,939; Prod Liab Occur, \$ 61,282; Earthquake, \$ 50,037; Inland Marine, \$ 58,332; Comm'l Auto Liab, \$ 14,685; All Other, \$ 6,108.

**Major 2004 Direct Premium Writings By State (\$000):** California, \$ 156,231 (24.2%); Florida, \$ 93,224 (14.5%); Texas, \$ 68,728 (10.7%); Illinois, \$ 42,235 (6.6%); New Jersey, \$ 27,492 (4.3%); 42 other jurisdictions, \$ 256,356 (39.8%); Aggregate Alien, \$ 293 (0.0%).

## FINANCIAL PERFORMANCE

The following text is derived from the report of ACE Westchester Specialty Group.

**Overall Earnings:** Returns on revenue and returns on policyholders surplus for the group have been strong for the past several years. The results of the past two years have additionally benefited from favorable market conditions. Since being acquired by ACE Limited, the group's steady increases in returns have outpaced peer group performance with five year average returns significantly higher than industry peers. A.M. Best expects the group's operating results to remain solid given the group's tight underwriting and pricing disciplines, conservative balance sheet rather well protected against pre-1997 adverse development through the NICO reinsurance cover, and the sound use of ongoing reinsurance placed with high quality reinsurers.

### PROFITABILITY ANALYSIS

Period Ending	Company				Industry Composite			
	Pretax ROR (%)	Return on PHS(%)	Comb. Ratio	Oper. Ratio	Pretax ROR (%)	Return on PHS(%)	Comb. Ratio	Oper. Ratio
2000	-99.9	-12.4	310.9	180.9	14.9	-12.4	108.9	81.8
2001	109.8	26.1	9.2	-27.6	3.7	-0.6	113.7	83.4
2002	52.2	22.6	50.2	42.5	9.7	4.2	95.0	79.6
2003	53.3	18.9	82.3	70.0	20.8	19.3	95.3	82.3
2004	44.3	18.1	67.7	42.5	15.2	12.1	94.6	82.9
5-Yr Avg	48.8	16.8	70.6	50.3	14.5	4.8	98.3	82.1
03/2004	49.7	XX	69.3	48.3	XX	XX	XX	XX
03/2005	51.7	XX	73.7	49.0	XX	XX	XX	XX

**Underwriting Income:** the group's combined ratios have been at or significantly below 100% for several years, the result of strict underwriting discipline, tight oversight of the claim process and a strong focus on minimizing administrative expenses. The results of the past two years have additionally benefited from favorable market conditions, with the slight increase in combined ratio in 2003 over 2002 resulting from a shift in the mix of business. A.M. Best believes that the group continues to be well positioned to benefit from the opportunities presented with changing market conditions and expects continued favorable operating results.

### UNDERWRITING EXPERIENCE

Year	Net Undrw Income (\$000)	Loss Ratios			Expense Ratios			Div. Pol.	Comb Ratio
		Pure Loss	LAE	Loss & LAE	Net Comm	Other Exp.	Total Exp.		
2000	-9,374	293.1	-29.6	263.5	8.3	39.2	47.4	...	310.9
2001	6,299	-33.8	19.6	-14.2	5.1	18.3	23.4	...	9.2
2002	15,579	17.6	18.2	35.8	8.3	6.1	14.3	...	50.2
2003	8,176	66.8	-7.4	59.4	6.1	16.7	22.9	...	82.3
2004	11,123	31.0	16.2	47.2	7.3	13.2	20.5	...	67.7

5-Yr Avg	...	41.6	8.4	50.0	7.2	13.4	20.6	0.0	70.6
03/2004	2,717	9.2	40.1	49.3	XX	XX	20.0	...	69.3
03/2005	3,003	38.7	8.5	47.2	XX	XX	26.4	...	73.7

**Investment Income:** The group's investment strategy has produced yields favorable relative to industry norms for several years and has significantly benefited the group's operating returns. The group's investment strategy is fairly conservative, with nearly 93% of total invested assets in long term bonds at December 31, 2003.

### INVESTMENT INCOME ANALYSIS (\$000)

Year	Company			Industry Composite	
	Net Inv Income	Realized Capital Gains	Unrealized Capital Gains	Inv Inc Growth	Inv Yield
2000	4,865	507	-180	(%)	(%)
2001	3,162	689	160	(%)	(%)
2002	2,669	43	20	(%)	(%)
2003	4,624	-159	...	(%)	(%)
2004	9,763	1,401	...	(%)	(%)
03/2004	1,900	1,377	...	(%)	(%)
03/2005	2,750	-846	-1	(%)	(%)

Year	Company			Industry Composite	
	Inv Inc Growth	Inv Yield	Total Return	Inv Inc Growth	Inv Yield
2000	(%)	(%)	(%)	(%)	(%)
2001	(%)	(%)	(%)	(%)	(%)
2002	(%)	(%)	(%)	(%)	(%)
2003	(%)	(%)	(%)	(%)	(%)
2004	(%)	(%)	(%)	(%)	(%)
5-Yr Avg	(%)	(%)	(%)	(%)	(%)
03/2004	XX	XX	1.6	XX	XX
03/2005	XX	XX	0.7	XX	XX

### INVESTMENT PORTFOLIO ANALYSIS

Asset Class	2004 Inv Assets (\$000)	% of Invested Assets		Annual % Chg
		2004	2003	
Long-Term bonds	262,895	97.9	81.4	57.8
Other Inv Assets	5,655	2.1	18.6	-85.1
Total	268,550	100.0	100.0	31.3

### 2004 BOND PORTFOLIO ANALYSIS

Asset Class	% of Total Bonds	Mkt Val to Stmt Val(%)	Avg. Maturity (Yrs)	Class 1 - 2 (%)	Class 3 - 6 (%)	Struc. Secur. (%)	Struc. Secur. (% of PHS)
Governments	32.9	1.5	4.0	100.0	...	...	...
States, terr & poss	16.6	0.1	8.3	100.0	...	50.4	33.8
Corporates	50.5	0.4	4.9	100.0	...	33.3	67.7
Total all bonds	100.0	0.7	5.1	100.0	...	25.2	101.5

## CAPITALIZATION

The following text is derived from the report of ACE Westchester Specialty Group.

**Capital Generation:** The group's level of internal capital generation has been solid since being acquired by ACE Limited. Strong underwriting results along with investment income from the group's fixed income portfolio have supported this growth. The group has made dividend payments to its parent company for several years. Over the past five years, dividend payments to the parent company, net of capital contributions received, have totaled \$90 million and are expected to continue in the foreseeable future. As a member of the well capitalized ACE Limited group, however, ACE Westchester also has access to additional capital from its parent, as necessary, to support growth. A.M. Best believes that the group continues to be well positioned to benefit from the opportunities presented with changing market conditions, resulting in performance that supports capital growth.

### CAPITAL GENERATION ANALYSIS (\$000)

Year	Source of Surplus Growth		Net Contrib. Capital
	Pretax Operating Income	Total Inv. Gains	
2000	-4,529	327	...
2001	9,445	849	...
2002	18,180	63	25,000
2003	20,103	-159	-5,000
2004	17,186	1,401	...
5-Yr Total	60,385	2,482	20,000
03/2004	4,493	1,377	...
03/2005	5,752	-846	...

Year	Source of Surplus Growth		PHS Growth (%)
	Other, Net of Tax	Change in PHS	
2000	949	-3,253	-11.7
2001	-4,113	6,181	25.1
2002	-8,758	34,485	112.0
2003	-12,380	2,564	3.9
2004	-21,014	-2,426	-3.6
5-Yr Total	-45,316	37,550	...
03/2004	460	6,330	9.3
03/2005	-1,401	3,505	5.4

**Overall Capitalization:** ACE Westchester maintains a very comfortable capital adequacy position as evidenced by its current BCAR score of 224. While the group's premium leverage is in line with the levels maintained by its peer group, gross and net loss reserve leverage is higher than the peer group averages. Ceded leverage is also above that of the group's peers. However, capital is protected by the NICO reinsurance cover which provides coverage for adverse loss development and uncollectible reinsurance. The potential recovery is equal to 75% of \$1 billion excess of carried loss reserves of \$721 million at December 31, 1996. At December 31, 2003, the remaining limit on the NICO reinsurance cover is \$600 million. A.M. Best expects the group's overall capitalization to continue to grow as management's successful business strategies continue to produce superior operating results.

### QUALITY OF SURPLUS (\$000)

Year	Year-End PHS	% of PHS			Dividend Requirements		
		Cap Stk/Contrib. Cap.	Other	Un-assigned Surplus	Stockholder Divs	Div to POI (%)	Div to Net Inc. (%)
2000	24,617	71.5	...	28.5	...	...	...
2001	30,798	57.2	...	42.8	...	...	...
2002	65,283	65.3	...	34.7	...	...	...

2003	67,847	62.8	...	37.2	-5,000	24.9	39.7
2004	65,420	65.1	...	34.9	...	...	...
03/2004	74,177	57.4	...	42.6	...	...	...
03/2005	68,926	61.8	...	38.2	...	...	...

### LEVERAGE ANALYSIS

Year	Company				Industry Composite			
	NPW to PHS	Reserves to PHS	Net Lev	Gross Lev	NPW to PHS	Reserves to PHS	Net Lev	Gross Lev
2000	0.3	1.5	2.4	5.9	0.4	0.8	1.4	2.7
2001	0.5	0.9	4.0	10.4	0.4	0.7	1.8	3.4
2002	0.7	0.5	2.8	9.5	0.8	0.7	2.5	4.3
2003	0.5	0.7	3.6	11.8	0.7	1.0	2.6	4.2
2004	0.7	0.8	5.0	17.1	0.7	1.0	2.4	3.9
03/2004	0.4	0.6	3.5	XX	XX	XX	XX	XX
03/2005	0.7	0.8	4.9	XX	XX	XX	XX	XX

Current BCAR: 152.2

### PREMIUM COMPOSITION & GROWTH ANALYSIS

Period Ending	DPW		GPW	
	(\$000)	(% Chg)	(\$000)	(% Chg)
2000	65,844	59.7	68,260	69.8
2001	178,597	171.2	182,500	167.4
2002	504,395	182.4	506,297	177.4
2003	530,247	5.1	530,437	4.8
2004	644,560	21.6	649,565	22.5
5-Yr CAGR	...	73.3	...	74.5
5-Yr Change	...	999.9	...	999.9
03/2004	126,666	9.9	127,841	11.0
03/2005	164,463	29.8	164,990	29.1
Period Ending	NPW		NPE	
	(\$000)	(% Chg)	(\$000)	(% Chg)
2000	6,861	219.9	3,742	67.9
2001	15,073	119.7	8,604	129.9
2002	47,171	212.9	34,822	304.7
2003	31,280	-33.7	37,747	8.4
2004	45,784	46.4	38,831	2.9
5-Yr CAGR	...	84.4	...	77.1
5-Yr Change	...	999.9	...	999.9
03/2004	9,335	-22.1	9,040	-29.9
03/2005	10,864	16.4	11,132	23.1

**Reserve Quality:** Conservative reserves are recorded by the group and reserves held on accident years since 1998 have developed redundantly in total by \$8 million from original loss reserve values. Reserves held at year-end 2002 developed redundantly in 2003 by \$34 million, the net effect of redundancies recognized for accident years 1996 and prior and for 2001 and 2002, somewhat offset by deficiencies recognized for accident years 1997 through 2000. The \$35 million redundancy adjustment to prior accident year reserves in 2003 was the net effect of a \$42 million redundancy in special property lines, a \$13 million deficiency associated with assumed non-proportional reinsurance and a \$5 million net redundancy for all other lines.

The group has established reserve levels for emerging environmental and asbestos claims that are consistent with industry standards given its paid loss activity. Based on Footnote 32 disclosure data, ACE Westchester reported \$245 million and \$171 million of gross and net A&E reserves, respectively, of which approximately two-thirds relates to asbestos exposures. This net

figure is exclusive of the cession to NICO under the pre-1997 accident year adverse development reinsurance agreement. The group's current A&E reserve position, which was strengthened in the current year, provides for a three year survival ratio of 21.3 x based on its historical paid loss activity related to these liabilities, which is stronger than many of its commercial umbrella lines peers. More importantly, the group is protected by the NICO reinsurance cover which provides coverage for adverse loss development and uncollectible reinsurance. The potential recovery is equal to 75% of \$1 billion excess of carried reserves of \$721 million at December 31, 1996. At December 31, 2003 the remaining limit on NICO's 75% participation in the reinsurance cover was \$600 million. The NICO cover is expected to minimize any earnings drag caused by adverse development arising out of A&E reserves.

### LOSS & ALAE RESERVE DEVELOPMENT: CALENDAR YEAR (\$000)

Calendar Year	Original Loss Reserves	Developed Reserves Thru 2004	Develop. to Orig. (%)	Develop. to PHS (%)	Develop. to NPE (%)	Unpaid Reserves @ 12/2004	Unpaid Resrv. to Dev. (%)
1999	23,427	25,640	9.4	7.9	999.9	11,757	45.9
2000	34,507	28,182	-18.3	-25.7	739.3	12,307	43.7
2001	23,886	23,855	-0.1	-0.1	277.2	12,768	53.5
2002	33,901	29,110	-14.1	-7.3	88.0	21,652	74.4
2003	42,674	37,160	-12.9	-8.1	94.1	30,915	83.2
2004	48,154	48,154	...	...	124.0	48,154	100.0

### LOSS & ALAE RESERVE DEVELOPMENT: ACCIDENT YEAR (\$000)

Accident Year	Original Loss Reserves	Developed Reserves Thru 2004	Develop. to Orig. (%)	Unpaid Reserves @ 12/2004	Acc Yr. Loss Ratio	Acc Yr. Comb Ratio
1999	631	1,812	187.2	649	101.0	124.2
2000	8,627	1,483	-82.8	550	64.5	112.0
2001	4,430	3,320	-25.1	461	63.9	87.3
2002	15,687	11,827	-24.6	8,884	43.7	58.0
2003	18,009	11,878	-34.0	9,263	38.5	61.4
2004	17,239	17,239	...	17,239	60.0	80.4

### CEDED REINSURANCE ANALYSIS (\$000)

Year	Company			Industry Composite			
	Ceded Reins Total	Business Retention (%)	Rein Rec to PHS (%)	Ceded Reins to PHS (%)	Business Retention (%)	Rein Rec to PHS (%)	Ceded Reins to PHS (%)
2000	84,962	10.1	227.8	345.1	46.9	94.8	125.7
2001	197,607	8.3	426.8	641.6	33.4	111.5	160.9
2002	438,147	9.3	366.7	671.2	40.8	129.3	179.8
2003	561,070	5.9	494.3	827.0	38.9	113.0	167.9
2004	794,542	7.1	872.5	999.9	43.0	107.9	147.2

### 2004 REINSURANCE RECOVERABLES (\$000)

	Paid & Unpaid Losses	IBNR	Unearned Premiums	Other Recov*	Total Reins Recov
US Affiliates	108,297	112,997	196,165	...	417,459
Foreign Affiliates	8,011	4,979	2,582	...	15,572
US Insurers	48,413	202,504	51,952	...	302,869
Pools/Associations	...	396	...	...	396
Other Non-US	49,280	158,332	44,357	...	251,969
Total (ex US Affils)	105,704	366,211	98,891	...	570,806
Grand Total	214,001	479,208	295,056	...	988,265

\* Includes Commissions less Funds Withheld



**Investment Leverage:** The group's non-investment grade bond leverage is high compared to its peers over the past three years due to a high yield bond strategy instituted at the beginning of the period. The group's high yield bonds are diversified by industry and issuer and include financial covenants that provide early warning signs of financial deterioration. The group currently does not have any material exposure to any single large investment and has positioned its portfolio to afford it the flexibility to take advantage of favorable yield curve opportunities. The group's investment strategy has produced yields favorable relative to industry norms for several years and has significantly benefited the group's operating returns. Total long term bonds constituted 93% of the group's total invested assets at December 31, 2003.

### INVESTMENT LEVERAGE ANALYSIS (% OF PHS)

Year	Class 3-6 Bonds	Company					Industry Composite	
		Real Estate/ Mtg.	Other Invested Assets	Common Stocks	Non-Affl Inv. Lev.	Affil Inv.	Class 3-6 Bonds	Common Stocks
2000	1.3	...	2.1	...	3.4	...	0.8	19.8
2001	1.6	...	0.1	...	1.7	...	1.2	17.5
2002	...	...	0.0	...	0.0	...	1.9	16.6
2003	...	...	...	...	...	...	1.3	18.1
2004	...	...	0.1	...	0.1	...	1.6	17.4

### LIQUIDITY

The following text is derived from the report of ACE Westchester Specialty Group.

Cash provided from premiums, investment income and portfolio maturities are reasonably predictable and normally exceed liquidity requirements for payments of claims and expenses. However, since the timing of available cash cannot always be matched precisely to commitments, imbalances may arise when demands for cash exceed cash on hand. Furthermore, a demand for cash may arise as a result of the group taking advantage of attractive investment opportunities and the group is expected to continue paying dividends to its parent. The group has been able to respond to these circumstances by maintaining an adequate supply of marketable securities which can be liquidated to meet temporary cash needs. In addition, as a member of the ACE Limited group, ACE Westchester's financial flexibility is enhanced by the parent's access to extensive financial resources.

### LIQUIDITY ANALYSIS

Year	Company				Industry Composite			
	Quick Liq (%)	Current Liq (%)	Overall Liq (%)	Gross Agents Bal to PHS(%)	Quick Liq (%)	Current Liq (%)	Overall Liq (%)	Gross Agents Bal to PHS(%)
2000	19.6	112.9	148.4	55.0	42.5	152.0	194.0	8.7
2001	27.7	81.9	129.9	111.6	34.5	133.9	168.4	11.0
2002	43.9	77.9	150.5	75.1	33.6	122.9	155.1	16.3
2003	77.2	147.6	136.9	79.7	34.0	118.5	154.3	14.6
2004	44.1	142.0	131.8	89.4	35.3	131.2	156.8	12.9
03/2004	XX	89.4	136.5	78.8	XX	XX	XX	XX
03/2005	XX	92.9	132.0	86.0	XX	XX	XX	XX

### CASH FLOW ANALYSIS (\$000)

Year	Company			Industry Composite		
	Underw Cash Flow	Oper Cash Flow	Net Cash Flow	Underw Cash Flow(%)	Oper Cash Flow(%)	Underw Cash Flow(%)
2000	-12,219	-8,915	-9,677	-99.9	-32.5	92.2
2001	31,393	33,000	7,621	242.9	238.4	76.7
2002	12,883	10,623	16,161	160.4	140.8	136.7
2003	21,029	22,658	10,983	144.3	139.6	219.3
2004	32,430	36,428	-33,655	197.3	200.9	191.9
03/2004	44,836	43,740	-33,601	-99.9	999.9	XX



03/2005

-134

180

-793

99.3

100.7

XX

XX

## HISTORY

This company was incorporated on June 30, 1971 in Hawaii as Industrial Insurance Company of Hawaii, Ltd., and began business on September 1, 1971. On November 30, 1994 the company redomesticated to Georgia by merger and changed its name to Westchester Surplus Lines Insurance Company.

Capital paid up is \$2,750,000, comprising 55,000 common shares at \$50 par value each. All authorized shares are issued and outstanding.

## MANAGEMENT

All of the outstanding capital stock is owned by ACE USA, Inc. (formerly known as Westchester Specialty Group, Inc.). The later is a wholly-owned subsidiary of ACE Holdings Inc., which is a wholly-owned subsidiary of ACE Limited. ACE Limited acquired ownership of the company and its parent on January 5, 1998 from Talegen Holdings, Inc., an indirect wholly-owned subsidiary of Xerox Corporation, Stamford, Connecticut.

**Officers:** Chairman of the Board, Brian E. Dowd; President, Dennis A. Cosby; Executive Vice Presidents, John M. Berger, Randolph D. Carey, David J. Lupica, Kathleen K. Morrison, Allen J. Sanderson; Vice President and Treasurer, Francis W. McDonnell; Vice Presidents, William N. Curcio, Robert J. Gaffney, William P. Garrigan, Geoffrey G. Gregory, John J. Lupica, James W. MacDonald, Paul G. O'Connell, Ed K. Ota, Jr., Susan M. Rivera, Joseph Stagliano, Charles E. Stauber, John P. Taylor, Edward D. Zaccaria; Secretary, George D. Mulligan.

**Directors:** John M. Berger, Randolph D. Carey, William N. Curcio, Brian E. Dowd (Chairman), Richard C. Franklin, Robert J. Gaffney, William P. Garrigan, Geoffrey G. Gregory, John J. Lupica, David J. Lupica, James W. MacDonald, Francis W. McDonnell, Kathleen K. Morrison, Paul G. O'Connell, Ed K. Ota, Jr., Susan M. Rivera, James B. Runyan, Otis L. Sanders, William V. Schmaltz, Charles E. Stauber, Edward D. Zaccaria.

## REGULATORY

An examination of the financial condition was made as of December 31, 2003 by the Insurance Department of Georgia. An annual independent audit of the company is conducted by PricewaterhouseCoopers, LLP. An annual evaluation of reserves for unpaid losses and loss adjustment expenses is made by Paul G. O'Connell, FCAS, MAAA, Executive Vice President and Chief Actuary, ACE INA.

## TERRITORY

The company is licensed in Georgia. It also operates on a surplus lines or non-admitted basis in the District of Columbia, Puerto Rico, AL, AK, AZ, AR, CA, CO, CT, DE, FL, HI, ID, IL, IN, IA, KS, KY, LA, ME, MD, MI, MS, MO, MT, NE, NV, NJ, NM, NY, NC, ND, OH, OK, OR, PA, SC, SD, TN, TX, UT, VT, VA, WA, WV, WI and WY.

## REINSURANCE PROGRAMS

The following text is derived from the report of ACE Westchester Specialty Group.

Reinsurance agreements are in force on all lines of business to manage net retained loss on individual policies and accumulations of net policy losses. TRIA coverage is retained at 10% after satisfying the TRIA event deductible.

On casualty lines, quota share reinsurance is purchased for primary general liability business. Treaty excess of loss and quota share reinsurance is purchased to maintain maximum net limits of \$4.5 million per policy for umbrella and \$6 million per policy for high excess business with attachments of \$25 million or higher..

Property business is protected with excess of loss reinsurance that reduced net limits to \$1.16 million per risk. Property catastrophe reinsurance is purchased to cover 95% of loss and expense to the 100-year PML net of per risk recoveries, in excess of a \$50 million retention. An additional \$200 million SuperCat layer is purchased to cover property catastrophe loss in excess of the

100-year PML.

Westchester entered into a stop-loss agreement with National Indemnity which provides protection against adverse development and uncollectible reinsurance. The potential recovery is equal to 75% of \$1 billion excess of carried loss reserves of \$721 million at December 31, 1996. At December 31, 2003 the remaining limit on NICO's 75% participation in the reinsurance cover was \$600 million.

## BALANCE SHEET (\$000)

<u>ADMITTED ASSETS</u>	<u>12/31/2004</u>	<u>12/31/2003</u>	<u>2004 %</u>	<u>2003 %</u>
Bonds	262,895	166,638	71.6	57.8
Cash & short-term invest	2,432	36,087	0.7	12.5
Other non-affil inv asset	81	...	0.0	...
Total invested assets	265,407	202,725	72.3	70.3
Premium balances	59,412	54,480	16.2	18.9
Accrued interest	3,142	1,874	0.9	0.7
All other assets	39,061	29,146	10.6	10.1
Total assets	367,023	288,224	100.0	100.0
<u>LIABILITIES &amp; SURPLUS</u>	<u>12/31/2004</u>	<u>12/31/2003</u>	<u>2004 %</u>	<u>2003 %</u>
Loss & LAE reserves	52,356	46,418	14.3	16.1
Unearned premiums	23,430	16,476	6.4	5.7
Conditional reserve funds	23,175	9,792	6.3	3.4
All other liabilities	202,642	147,691	55.2	51.2
Total liabilities	301,603	220,377	82.2	76.5
Capital & assigned surplus	42,613	42,613	11.6	14.8
Unassigned surplus	22,807	25,234	6.2	8.8
Total policyholders' surplus	65,420	67,847	17.8	23.5
Total liabilities & surplus	367,023	288,224	100.0	100.0

## SUMMARY OF 2004 OPERATIONS (\$000)

<u>STATEMENT OF INCOME</u>	<u>12/31/2004</u>	<u>FUNDS PROVIDED FROM OPERATIONS</u>	<u>12/31/2004</u>
Premiums earned	38,831	Premiums collected	65,753
Losses incurred	12,044	Benefit & loss related pmts	21,448
LAE incurred	6,296	Net transfers to accounts	...
Undrw expenses incurred	9,368	LAE & undrw expenses paid	11,875
Net underwriting income	11,123	Undrw cash flow	32,430
Net investment income	9,763	Investment income	10,480
Other income/expense	-3,700	Other income/expense	-3,700
Pre-tax oper income	17,186	Pre-tax cash operations	39,210
Realized capital gains	1,401	Income taxes pd (recov)	2,782
Income taxes incurred	6,549	Net oper cash flow	36,428
Net income	12,038		

## INTERIM BALANCE SHEET

ADMITTED ASSETS  
Cash & short term invest

03/31/2005  
1,639

Bonds	263,868	...	...
Other investments	536	...	...
Total investments	266,043		
Premium balances	60,143	...	...
Reinsurance funds	49,910	...	...
Accrued interest	1,680	...	...
All other assets	2,369	...	...
Total assets	380,146		
<b>LIABILITIES &amp; SURPLUS</b>	<b>03/31/2005</b>		
Loss & LAE reserves	53,399	...	...
Unearned premiums	23,161	...	...
Conditional reserve funds	23,175	...	...
All other liabilities	211,485	...	...
Total liabilities	311,220		
Capital & assigned surp	42,613	...	...
Unassigned surplus	26,313	...	...
Policyholders' surplus	68,926		
Total liabilities & surplus	380,146		

### INTERIM INCOME STATEMENT

	Period Ended 3/31/2005	Period Ended 3/31/2004	Increase/ Decrease
Premiums earned	11,132	9,040	2,092
Losses incurred	4,314	834	3,480
LAE incurred	944	3,625	-2,680
Underwriters expenses incurred	2,872	1,864	1,008
Net underwriting income	3,003	2,717	285
Net investment income	2,750	1,900	850
Other income/expenses	...	-124	124
Pre-tax operating income	5,752	4,493	1,259
Realized capital gains	-846	1,377	-2,223
Income taxes incurred	1,174	2,178	-1,004
Net income	3,733	3,693	40

### INTERIM CASH FLOW

	Period Ended 3/31/2005	Period Ended 3/31/2004	Increase/ Decrease
Premiums collected	20,399	43,407	-23,009
Benefit & loss related pmts	17,244	-3,553	20,797
Undrw expenses paid	3,288	2,125	1,163
Underwriting cash flow	-134	44,836	-44,969
Investment income	4,803	2,357	2,445
Other income/expense	...	-124	124

Pre-tax cash operations			
	4,669	47,069	-42,400
Income taxes pd (recov)	4,489	3,329	1,160
Net oper cash flow	180	43,740	-43,560

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